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## THE BANKS AND THE PANIC OF 1893.

IN considering the relations of American banking to the panic of 1893, the first and most serious question is, how far, if at all, defective bank management was responsible for the collapse. History has ascribed two of our greater panics — those of 1837 and 1857 — largely to reckless banking. But the banking system itself, its regulation by the state and the spirit in which the system is administered have undergone great and salutary changes since those days. It is the popular belief that the “wild-cat” bank-notes, ill-secured and over-issued, were in these earlier panics the sole cause of mischief. This, however, is not strictly true; and a study of the facts will show that despite the careful restrictions of the present system, enough factors of danger still remained in 1893 to make the whole business community vulnerable. Circulating notes are not the only or the easiest means by which the banks may bring about business inflation. Deposits inscribed on the books of banks, like bank-notes in circulation, represent credit entrusted to the banks by outside capital. In both cases the credit fund is absorbed in loans or other bank investments; in both the bank pledges return in actual money on demand. Excessive and unsecured bank-note issues were indeed a peculiarly vicious form of bank inflation, in that they cheated the poor and ignorant, who accepted the notes only because the notes to them were money, and who never consciously took their chances with an institution’s solvency. But otherwise over-expansion, always through excessive encouragement of loans, has in each case substantially the same result. Bank-notes, the total issue of which had for years been contracting, and the security of which is now perfect, were not a factor in last summer’s panic. But the volume of the bank-deposit fund, no less than the security maintained for its redemption, is a matter for investigation.

As regards this fund, a remarkable change in bank conditions has taken place during the last two decades. Comptroller Hepburn said, in his report of 1892 :

In the sixties banks did business on their capital ; supplied the wants of customers and earned their dividends with the money which shareholders subscribed. Now capital is made just sufficient to command public confidence. Usually a large surplus is accumulated, but the business is done upon depositors' money.

The general truth of this criticism may be made apparent by a comparison of the figures. Bank capital has indeed increased heavily in the last two or three decades ; but the increase in the bank-deposit fund has far outstripped it. In 1870 the combined account of national bank capital, surplus and undivided profits was 37 per cent of total liabilities. In 1879 this percentage was 33 ; at the close of 1892 it had fallen to 29. In 1870 the individual deposits alone made up only one-third of the total liability account ; in 1879 they constituted 39 per cent ; in 1892 they were more than half.<sup>1</sup> The national banks' own funds exceeded individual deposits in 1870 ; in 1892 their proportion to such deposits was less than 58 per cent. Such compilations as have been made of the state bank balance-sheets show that the contrast there between the two banking epochs is even more remarkable.<sup>2</sup>

Now it is perfectly true that this change in banking methods came in response to a genuine and extraordinary development of the country's industrial resources. It is true, also, that this expansion in bank deposits arose in the main from the immense inflow of home and foreign capital into American investments,

<sup>1</sup> The figures at these three dates were as follows :

|                            | 1892.           | 1879.         | 1870.         |
|----------------------------|-----------------|---------------|---------------|
| Capital, <i>etc.</i> . . . | \$1,044,233,834 | \$617,501,367 | \$576,118,173 |
| Individual deposits        | 1,764,456,177   | 755,459,966   | 507,368,619   |
| Total liabilities . .      | 3,480,349,667   | 1,925,229,617 | 1,538,998,106 |

<sup>2</sup> Returns compiled by the comptroller's office at Washington show percentage of state bank capital, surplus, *etc.*, to total liabilities to have been 40 in 1879 and 32 in 1892. Proportion of the same to individual deposits was 75½ in 1879 and 50 in 1892. This is not, however, a complete exhibit, since only 616 state banks were accounted for in 1879, and by no means all in 1892. As late as this year, ten states and two territories had no organized banking department, and made no returns.

especially since the specie resumption of 1879. Nevertheless, it will hardly be denied that so vast and disproportionate an extension of the purely credit element in banking could not fail, except under most experienced guidance, to relax the principles of conservative bank financiering, and at the same time necessarily to increase business risk. The general principle of trade, that the smaller the capital relative to the total obligations, the greater the chances of disaster, certainly does not fail of application here. Borrowers, indeed, in other lines of industry, whose credit obligations are chiefly placed on time, have at least a breathing-space in a period of panic. The bank, whose liabilities, outside of its own funds, are practically all demand, has not even this advantage. Even "quick assets," such as may be resorted to for sudden liquidation of liabilities, are but a small proportion of the total bank resources, and in the Western banks are insignificant.<sup>1</sup>

There is, of course, one highly important safeguard in the banking business, which most other credit enterprises lack. The national bank law and the state laws, wherever proper state bank legislation has been effected, strive to reduce the risk by stringent requirements of a percentage cash reserve against deposits. It is true that in our country this minimum requirement is low. Nevertheless, it is conceivable that under certain conditions even such light restrictions would ensure not only safety to depositors, but conservatism in the banks' own attitude towards borrowers. These conditions are, a properly regulated national currency and a *bona-fide* maintenance of bank reserves—not, as our present laws permit, a reserve of which a three-fifths part, in the most vulnerable bank communities, may be shipped away for deposit in a distant city. Had these two conditions ruled in our recent financial history,

<sup>1</sup> The surest "quick asset" is, of course, a demand loan on first-class collateral. At the close of 1892, out of the \$2,153,498,829 national bank loans reported to the comptroller, only \$369,248,604, or less than eighteen per cent, were placed on demand. Of these, moreover, only \$273,328,289 were secured by collateral. In New York city alone, where the total of loans was \$344,199,941, demand loans on stock or other collateral were \$117,751,227, or sixty-five per cent of the country's total.

recklessness or dishonesty in banking might indeed have come to light, some dangerous stimulation of the speculative spirit might have been witnessed, with resulting losses and reaction ; but such a tearing down of the whole financial structure as was seen last summer would have been perfectly impossible.

Unfortunately, the currency policy of the United States government has always been such as completely to prevent the application of any such general check. The coinage of over-valued silver dollars since 1878, and the issue of Treasury notes on silver bullion since 1890, have actually increased the country's silver and paper circulation, between 1879 and 1894, by seventy-five per cent. Not a dollar of this new currency was available for exchanges in foreign trade. Hence, it heaped up at all times in the city bank reserves, and in dull years lay idle even in the reserves of country institutions. As a result, the cash reserve requirement, as a check on reckless trade inflation, became almost wholly nugatory. A borrower of doubtful credit or with questionable collateral will always offer tempting rates, but he is not a serious menace to the general system when the legitimate demand is heavy, or when the loanable funds in bank are low. Under our clumsy laws, the currency supply, and hence the actual money fund in bank, are often largest when demand from trustworthy borrowers is least. In active times these conditions force unhealthy and violent extremes ; in dull times they offer a premium on bad loans, such as figured in shocking quantities in the bankrupt asset lists of 1893.

It was on the Western banks that the shock of panic fell in 1893 with greatest violence. The records of no previous panic show in this regard such impressive sectional contrasts. The list of national and state bank failures for 1893 shows for the New England and Middle Atlantic states seventeen suspensions, with total estimated liabilities of \$13,138,073. This list includes such financial centres as New York, Boston and Philadelphia. On the other hand, the failures of similar institutions in the five states of Ohio, Indiana, Illinois, Michigan and Wisconsin numbered forty-nine, with aggregate

liabilities of \$23,163,537. In the eleven granger and Rocky Mountain states, still further to the west, the state and national bank failures reached the yet more disproportionate number of 147, and reported liabilities footed up no less than \$24,781,181.<sup>1</sup> Taking the country as a whole, the record shows that out of 360 national and state banks suspended during 1893, with liabilities of \$109,547,556, no less than 343 failures, with liabilities of \$96,409,483, occurred in sections of the Union west or south of Pennsylvania. The failures of private banks and savings institutions were distributed in almost exactly the same proportion.<sup>2</sup>

For this remarkable disparity there were several reasons. Rapid development on other than local capital had been the chief feature of the West's recent career, and this was a double element of weakness. The collapse of the "land booms" in 1889 and 1890 had served as a wholesome check to speculation, but the two enormous grain harvests of 1891 and 1892 had again revived it. The warnings of 1890 and of the brief succeeding period fell in that section on deaf ears. The evils of a vicious currency took root for this reason far more extensively west of the Ohio. "Bad loans" made up a startlingly large proportion of the assets of bankrupt institutions. The East, on the other hand, where foreign capital was concentrated, felt much more severely the shock and the significance of the London crash of 1890. When, in 1891, the expulsion of gold by our accumulated paper currency began, it was the Eastern banks from whose vaults the gold was first withdrawn to meet such export requirements. It was through these banks that the "run" began, with 1893, on the government's gold reserve for the redemption of legal tender notes. It was on the Eastern stock exchanges that foreign investors poured for two years continuously their holdings of American securities. These multiplied signs of coming trouble were not ignored. The Eastern institutions were indeed subjected to the same demor-

<sup>1</sup> Figures compiled and published by Dun's Mercantile Agency.

<sup>2</sup> Total failures of such institutions in 1893 were 250; liabilities, \$41,895,346. Outside of the New England and Middle Atlantic states failures were 224; liabilities, \$35,543,801.

alizing pressure from currency over-issues, and they furnished their share of reckless ventures and dishonest speculation. But the weeding out of such concerns was very thorough in 1890 and in the ensuing year or two, and, as a rule, the policy of the Eastern city banks on the eve of the general breakdown was sound and conservative.<sup>1</sup>

But all this relative conservatism in the Eastern banks failed to offset the results of a thoroughly dangerous practice embodied in our banking system. This is the carrying and loaning out, in city banks, of interior banks' legal reserves. This account, which Professor Amasa Walker aptly described as the most "explosive" element in American banking, arises from the larger opportunity offered in great financial centres for the steady use of capital. At nearly all times Western banks are glad to get the two per cent allowed for use of their deposits by Eastern institutions. The national bank law, moreover, permits the so-called "country banks" to deposit with other banks in certain specified cities three-fifths of their fifteen per cent cash reserve. Since the country banks can at no time legally lend out this last-named fund, it is kept, as might be supposed, perpetually on deposit with the reserve city institutions. In recent years this trust fund has reached phenomenal proportions. At the close of 1892, the national banks reported "due from approved reserve agents" the sum of \$204,948,159. The total amount due from other banks was more than double this. In May of 1892 the New York City banks alone held \$293,078,195 subject to call from other institutions. Let it be noted not only that this fund was money belonging to private depositors in other banks, and subject to their instant call, but that a large proportion of it was the very money prescribed by law to be held for the purpose of meeting "runs" by the Western banks' own creditors.

<sup>1</sup> The truth of this was illustrated when New York's bubble of speculation in the "industrial stocks" broke in May. This group of stocks fell on the average twenty-five points within a week, and some of them forty or fifty, but no bank suffered. This was, moreover, before the issue of loan certificates. As a matter of fact, the banks had long been notoriously shy of these securities.

This will explain the violence of the strain on city banks when the country institutions all at once took fright.

Nor were the bad results of the system by any means confined to cities whence interior deposits were withdrawn. The city depositories kept on hand by law a cash reserve of twenty-five per cent. The country banks held in their vaults only the insignificant reserve of six per cent. Grant, what was generally true, that the city banks were conservative in their use of deposited interior reserves, and invested them as a rule in demand loans on stock or bond collateral. A bank in Iowa or Colorado, with its three-fifths reserve deposited in New York City, may easily enough, when panic threatens, telegraph an immediate call for the return of such deposits. But actual money, even if ready for delivery, cannot be shipped from New York to Denver in a day, and forty-eight hours' delay may easily settle the fate of the Western institution. This is the reason why so many banks throughout the West suspended in last summer's crisis, when they were perfectly solvent on their books, and indeed resumed payments in a few days' time—as soon, in fact, as the money shipped from their reserve depository reached them.<sup>1</sup> The whole practice, in a country of such vast distances as ours, is full of continual possibilities of mischief. Whether or not a serviceable reserve-deposit plan with better safeguards could be devised, I shall not here discuss. But it is worth our while to note that the Bank of England, the most conspicuous of all depositories of tributary bank funds, carries in its entire deposit liabilities a less amount than our Eastern banks hold from deposits of interior reserves alone. In England delay in transferring currency against withdrawals by interior banks reaches a minimum. Yet the Bank of England habitually

<sup>1</sup> The comptroller reports that out of the total of 158 national bank failures, with a capital stock of \$30,350,000, eighty-six, with a capital of \$18,205,000, resumed business within a short time. None of the five banks which suspended in the New England and Middle States resumed payment. Of the six national banks which suspended in Iowa, all but one subsequently resumed. Sixteen national banks suspended in Colorado, of which all but two resumed, and six respectively in Oregon and California, of which in each case all but two resumed.

holds against its total deposits a cash reserve of forty to forty-five per cent, and even now Mr. Walter Bagehot's argument is being repeated by a score of excited London critics, that the Bank, as depository for other institutions, is in the nature of a public trustee, whose directors must content themselves wholly with ultra-conservative investments and with profits below the average.

The facts undoubtedly make it hard to say exactly how far the banks as a whole were culpable in this inflation process, or how far they were themselves victims of outside circumstances. Both conclusions will be found in many cases correct. When we discuss, however, the conduct and policy of the banks after the panic of 1893 had actually begun, we stand on firmer ground. Every banking institution has its own peculiar responsibility placed upon it in time of panic, but the gravest responsibility by far rests on the great city depositories. In 1857, in 1861 and in 1873, the banks of the leading Eastern cities were the first to set an example of general suspension. With one noteworthy exception—the maintenance of payments by the Chicago banks in 1873—the panic record of our city banks, up to the last ten years, is a discreditable chapter of nerveless fright and easy surrender. It is, therefore, a gratifying fact to recognize, that though the violence of panic shock in 1893 was greater than in any preceding year, no general bank suspension followed, and in the Eastern cities no suspension whatever except as a result of actual insolvency.

Nor is this all that can be said in praise. The reserve cities furnished throughout the crisis a memorable exposition of the principles of sound panic banking. The time-honored rule, established by the "Bullion Report" to Parliament in 1810, that in time of panic banks should discount freely and fearlessly for all solvent customers, was observed in a remarkable degree. In New York City, in ordinary times, the loan account often falls far below the deposit total;<sup>1</sup> it rarely exceeds it.

<sup>1</sup> In the first week of 1893, New York clearing-house bank loans were \$441,283,700; deposits \$455,367,800. In the last week of 1893, loans were \$417,606,900; deposits \$506,437,800.

Between June 4, 1893, the week when panic may be said fairly to have begun, and August 5, which may be called the height of actual panic, deposits in the sixty-four New York clearing-house banks decreased \$58,466,000, and actual specie and legal tender holdings \$49,621,800. This was a terribly sudden and violent impairment of reserves, the actual money decrease being thirty-eight per cent. Yet in the face of it, outstanding loans were contracted only \$7,972,700. This remarkable maintenance of bank accommodation to borrowers, in the face of monetary crisis, was made possible by two distinct and wise measures of policy. The first was a firm and continuous curtailment of outstanding loans before the panic's actual outbreak.<sup>1</sup> This was to strengthen cash resources and reduce pressing liabilities. The second measure was the adoption, when once real panic had begun, of a policy almost exactly opposite.<sup>2</sup> This was the issue of clearing-house certificates, in order to maintain the loan account.

I shall not enter into a lengthy discussion of this financial contrivance. It is enough to say that the loan certificates are a purely American invention, and that their safe and satisfactory operation in four severe financial crises<sup>3</sup> has won for the

<sup>1</sup> Between the first week of April and the first week of June, loans were reduced in New York \$16,834,300, although in the same time the total cash reserve increased \$8,304,700, and the surplus reserve over the required twenty-five per cent of net deposits \$10,324,425.

<sup>2</sup> The banks followed another thoroughly sound principle in lending only at high rates; the sufficient reason being that a high rate is a matter of no concern to a borrower in real extremity, while a low rate is a temptation to unscrupulous borrowers to engage the money and then relend it at a rate fixed by the needs of others. The banks were therefore entirely right in lending at one-eighth per cent and interest, or fifty-one per cent, yearly, the five millions later obtained through loan certificates and released in preparation for gold imports. An effort then to "break" the money market by offers at a low rate would have had extremely bad results. So, in the ensuing week, the action of the New York banks in raising the rate for interior re-discounts to twelve per cent was fully justified. Both actions have ample precedent in the skillful financing of the Bank of England during the Baring crisis of November, 1890.

<sup>3</sup> They were issued in 1873, in 1884, in 1890 and in 1893. In 1873 New York issued \$26,565,000, and Philadelphia \$6,785,000. In 1884 New York alone issued certificates, the maximum being \$24,915,000. In 1890 New York issued \$15,205,000, Philadelphia \$8,870,000, and Boston \$5,065,000. In 1893 New York issued \$38,280,000, Boston \$11,445,000, Philadelphia \$10,965,000, Baltimore

system the approval of practically all competent judges. They are, as is generally known, a species of currency issued by a clearing-house committee to all banks in the association applying for such accommodation and furnishing approved and sufficient collateral. These certificates are by agreement accepted in payment of balances between banks of the clearing house. They cannot, of course, circulate outside the limits of this clearing house; and an annual interest rate of six per cent, charged up daily against the bank in whose name such certificates are outstanding, insures their early redemption when the money market is restored to equilibrium.

Through the use of this ingenious emergency-device last summer, solvent borrowers were protected by the courageous advance of banking credits at the very worst hour of panic. Nor were the system's benefits extended to individual borrowers alone. Not only did the interior banks, at the panic outbreak, call in from city institutions a great part of their own deposited reserves, but they were clamorous for "re-discounts"; in other words, for the purchase from them for cash of paper already discounted for their own customers. To this demand, too, which came with no impropriety from heavy depositors, the larger banks responded. The total of notes and bills re-discounted for other institutions rose from \$14,021,596 in March to \$18,953,306 in May, and to \$29,940,438 in July, the height of the summer's panic. In 1873, during a corresponding panic period, the account increased only from \$5,403,043 to \$5,987,512.

The clearing houses of four other cities followed New York's example in the issue of loan certificates. Chicago, however, where a strong local prejudice exists against the plan, refused to follow. In the worst of the August panic, a resolution authorizing such issues was indeed adopted by the Chicago

\$1,475,000, and Pittsburg \$987,000. The average time between the first issue and final cancellation of the certificates is about four months. The real origin of the plan was in the action of the New York clearing house in 1857, when certificates of credit were issued through the Metropolitan Bank to state banks which could not redeem their notes; the notes being deposited as security against the certificates.

clearing house, but no bank availed itself of the opportunity. The result was exactly what might have been foreseen. In the Eastern cities the use of loan certificates so far offset the violent shrinkage in reserves, that between May 4 and July 12 the loan account of the New York national banks actually increased; the loans of Philadelphia were cut down only two per cent, and those of Boston only four per cent. But Chicago, lacking the emergency provision of the Eastern clearing houses, was forced to reduce its loans no less than fifteen per cent.<sup>1</sup> In a city where local enterprises were already inflated by speculation incident to the World's Fair, the result of this contraction was a collapse more violent than that of any other large commercial centre.

Another highly important outcome of the loan-certificate issues deserves discussion. In a panic caused or intensified by the actual hiding away of money, the most obvious measure of relief might seem to be the raising of loans in other countries, and the importation thence of gold to make good impaired reserves. This operation, however, is not as simple as it looks. Foreign capitalists are rarely disposed to lend in a nation or city where the whole financial structure is shaking. If indeed they could be induced to buy securities or commod-

<sup>1</sup> The following figures, taken from the national bank reports as compiled by the comptroller, illustrate the changes :

|                           | NEW YORK.     |                 | BOSTON.       |                 |
|---------------------------|---------------|-----------------|---------------|-----------------|
|                           | <i>May 4.</i> | <i>July 12.</i> | <i>May 4.</i> | <i>July 12.</i> |
| Loans . . . . .           | \$307,372,243 | \$308,646,935   | \$142,975,348 | \$137,484,412   |
| Specie and legal tender . | 98,086,692    | 76,719,353      | 14,384,581    | 12,869,552      |
| Individual deposits . . . | 286,985,310   | 246,736,851     | 98,125,482    | 89,711,636      |
| Due other banks . . . .   | 168,483,706   | 155,507,227     | 37,713,052    | 36,956,918      |
|                           | PHILADELPHIA. |                 | CHICAGO.      |                 |
|                           | <i>May 4.</i> | <i>July 12.</i> | <i>May 4.</i> | <i>July 12.</i> |
| Loans . . . . .           | \$96,655,813  | \$94,515,532    | \$96,824,857  | \$82,420,381    |
| Specie and legal tender . | 20,533,549    | 17,238,715      | 29,273,025    | 24,862,382      |
| Individual deposits . . . | 95,489,471    | 89,042,095      | 75,781,074    | 66,433,367      |
| Due other banks . . . .   | 22,791,614    | 22,241,136      | 48,856,591    | 36,931,031      |

The contraction of loans in Chicago was far more violent later in July and in August, dates not covered by the national reports. The Chicago banks themselves publish no statements except when called for by government authorities.

ities in amounts exceptionally large, gold would be normally due in payment. But the trouble is, that foreigners, like all other sagacious speculators, are likely to wait until they are sure that prices have "touched bottom"; which usually means that they will wait until too late for timely relief. There have, indeed, been gold importations in panic years. As long ago as 1838, foreign merchants and bankers in New York borrowed £1,000,000 gold from the Bank of England, to repair the shattered local bank-reserves. The London bank itself, in the same year, relieved a similar distress in London by a loan of £2,500,000 from the Bank of France. More than half a century later, in November, 1890, the Bank of England averted panic by a series of operations, all of which hinged on the importation of £5,000,000 gold borrowed from the banks of France and Russia. In this memorable episode, the gold shipment was so distinctively an operation in the loan market that within six months the Bank of France received back its gold in the very receptacles in which it had been conveyed to London.<sup>1</sup>

Of all these importations, however, only one—that of the English bank in 1890—was made early enough to forestall, through restoration of public confidence, the worst mischief of panic. Yet in every serious money panic—including that of 1873, when specie imports were at no time a factor of real significance—foreign exchange rates have fallen and remained materially below the normal gold-importing point. The reason for this is obvious. The blocking of the American money market equally blocks the market for sterling bills. In their eagerness to raise funds for pressing needs, exporters of

<sup>1</sup> It is not, perhaps, generally known that the £3,000,000 gold loan of November, 1890, from the Bank of France, was secured by the deposit of short-dated British Treasury bonds; these bonds having been furnished the Bank of England by Mr. Goschen, then chancellor of the exchequer, in temporary exchange for national debt stock. This was to comply with certain business rules of the Bank of France. Paris exchange on London rose a week before this transaction to 25 f. 40 c., eight centimes above the gold-exporting point. The cost in charges of the entire £5,000,000 continental gold importation was £100,000, besides interest. Before this negotiation was closed, the government offered Mr. Lidderdale, governor of the Bank of England, the option of a suspension of the Bank Act of 1844. The offer was wisely declined.

merchandise offer their bills at any sacrifice, but find no market, because the mercantile importers, who ordinarily furnish the demand, cannot now raise the money to pay for their remittances. At times (as in 1873) this pressure of unmarketable bills weighs down sterling quotations to a level absurd and almost senseless ; yet the market continues blocked. This was the case in 1893, up to the last week of July. Until the July panic reached its crisis, nobody seems to have thought of clearing-house loan certificates as a means of breaking the sterling dead-lock. It was indeed argued, even by members of the clearing-house committee, that gold imports ought not to be "forced." This is a sound enough principle, though it is rather hard to understand how such exports could be "forced" at any time, except by the counter-sale of something else at a sacrifice. But however that may be, the sudden contraction of our currency, through the money hoarding, had completely upset such rules, both practically and theoretically. What was needed was instant relief from panic. Purchase of foreign gold would accomplish this, and would do it while merely hastening shipments which could be paid for later either by the return of the borrowed gold (as in the Bank of England's operation of 1890), or by repayment in securities and produce (as was the case with us later in 1893).

Our bank presidents seem to have been at first in doubt as to the practicability of this expedient. By such delay three weeks at least of precious time were lost.<sup>1</sup> At length, in the week beginning July 24, when the Erie Railroad failed, the Milwaukee Bank closed its doors, and panic became such that the stock-exchange governors were discussing the shutting up of the exchange, the matter came to a head. Three bank presidents of New York City appealed to the head of a prominent gold-shipping house, to know if it was not possible to buy gold in London and import it. The answer was : "Furnish the credits here in New York and you shall have the gold." The requisite credits were instantly obtained through a heavy

<sup>1</sup> Rates for demand sterling bills sold below the normal gold-importing point before the close of June, and during July did not rise above it.

issue of clearing-house loan certificates, and within twelve hours upwards of \$5,000,000 gold had been obtained in London.<sup>1</sup> This simple operation proved, as it had proved three years before in London, to be the turning-point of panic. The stock market rose rapidly, and never subsequently fell into demoralization. But too much mischief had been done already to restore financial equilibrium in a day, or by a single importation. So extreme, indeed, was the need for actual money, especially in the Western States, that this discovery of the sterling market's possibilities started a buying movement in exchange sudden and violent enough to drive the rates, within a week, actually above the normal gold-exporting point. Even this did not for an instant check the import movement. In August and September \$48,000,000 gold came in from Europe; and though the enormous sales of stocks and wheat to foreigners later depressed the sterling market, over \$10,000,000 gold was ordered in London while rates were quoted here above the export level. The importance of this precedent, with a view to possible future emergencies, can hardly be overestimated.<sup>2</sup>

It has been said already that there was no bank suspension in the reserve cities during 1893, except where the strain of panic forced public insolvency. This statement needs, however, one important qualification, involving discussion of a very delicate and unpleasant question. It will be remembered by those who watched the course of panic financiering, that accumulations were freely made, as early as July, that banks were refusing cash payments to large depositors. At first the

<sup>1</sup> So simple was this operation, that the gold practically cost the banks nothing beyond the six per cent interest paid on the loan certificates. The firm of Lazard Frères charged the bankers, as commission, only three per cent for five days.

<sup>2</sup> I have not mentioned the taking out of new bank-note circulation, because this was not a prominent factor in the real relief of the money market, and because it is not likely to remain a possible emergency factor. The city banks were, however, extraordinarily slow in making use of this obvious and, under the existing law, perfectly proper means of relief. Between July 1 and October 1 the national banks as a whole took out \$24,977,637 new circulation; of which increase approximately \$9,000,000 was issued to the banks of New York City. Of this \$9,000,000 the greater part was not issued till after September 1st, a fact for which the delay in printing notes at Washington only partly accounts.

country banks were charged with refusing to remit their cash collections.<sup>1</sup> Banks in some larger cities were next accused of withholding similar remittances. At length it was alleged, in the daily press and on the floor of the United States Senate,<sup>2</sup> that New York City banks were refusing to redeem checks of their own depositors in legal tender money. This accusation was made with bitterness, and it was not denied. The popular sentiment was, however, strongly against the proposed senatorial investigation. No bank depositor to whom cash payment was refused ever gave public utterance to complaint. No legal process was invoked. The newspaper critics soon found their attack on the banks impolitic. The Senate resolution for an inquiry was referred to the finance committee, where it was smothered, as it ought to have been and every one knew it would be, and there can be no doubt that its advocates paid the penalty of their aggressiveness in a considerable loss of popularity. Thus far, then, it might be argued that public opinion sustained the action of the banks in question.

From an economic standpoint, however, this by no means ends the matter. That some of the New York clearing-house banks did thus suspend cash payments, is a matter of public knowledge. No formal or concerted action, indeed, was taken by the banks; the clearing house ignored the whole performance; the majority of New York institutions continued to pay cash on demand to all depositors, and those which did refuse cash payments not only offered to such depositors checks on

<sup>1</sup> Some novel and curious incidents arose in this connection. The express companies did a very large business, during the panic, in presenting out-of-town checks at the banks on which they were drawn, and bringing the money to the city bank whence the check was remitted. The out-of-town banks frequently resisted this by paying in silver dollars or fractional coin. Domestic exchange between two great Eastern cities was at one time fixed by the express charges for transporting silver dollars. On August 30, Chicago exchange on New York sold at three dollars premium per \$1,000.

<sup>2</sup> In the debate on Senator Peffer's resolution of August 22, instructing the comptroller of the currency to inform the Senate whether certain New York banks were or were not violating the National Bank Act by refusing cash to depositors, and by charging exorbitant discount rates. The resolution was advocated by Senator Hill, and opposed by Senators Hoar, Gorman, Hawley and others.

other banks,<sup>1</sup> but cashed small checks without inquiry, and larger checks when the need was shown to be imperative. This was undoubtedly a vast improvement over the general shutting-down of 1873. Nevertheless it was suspension, its effect on business and credit was mischievous in the extreme, and it can be justified only on the plea of absolute necessity.

This plea, in my opinion and in the judgment, I believe, of the soundest clearing-house authorities, is quite untenable. The issue of loan certificates was a recourse still open to every solvent bank, and the banks which did shut down on cash payment to depositors included several of the soundest institutions in the city. July's shipments of currency, to meet deposit withdrawals of interior banks and other institutions, were indeed extremely heavy, but on August 5 there was still left in the New York clearing-house bank-reserves \$79,218,500 specie and legal tenders. Moreover, at the very time when banks resorted to such partial suspension, importation of gold from Europe had begun. Any bank with securities on which to take out loan certificates was able, within seven days, to replace such certificates in American gold coin.<sup>2</sup>

But the plea of necessity was not the bankers' only plea. It was openly argued that the restriction on cash payments had positively good results, in that it stopped withdrawals by money hoarders. Let us observe what were the actual results of this restriction. It was followed by a market phenomenon unfamiliar to the present generation. Currency, as the phrase was, went to a premium. Two or three active Wall Street money brokers at once inserted newspaper advertisements offering a premium for gold or silver coin, or for paper legal tender currency. This premium was at first one and one-half

<sup>1</sup> Most of these banks sent to their customers rubber stamps marked "payable through the clearing house." This was to be stamped on checks when drawn, by way of a polite and euphemistic hint to receivers of the checks that the bank declined to pay cash.

<sup>2</sup> Owing to the foolish action of our Treasury Department in March, 1891, based on an equally foolish Congressional amendment offered by Senator Sherman, a charge of forty cents per \$1,000 had been imposed on gold bars taken for export. As a result, most of the \$155,000,000 net gold exports from the United States since that time were of American coin.

and two per cent ; it rose once to four per cent. In quick response to these advertisements, the hoarded money of New York and its vicinity poured into the Wall Street offices. The brokers paid for this currency, in turn, by certified checks on their own bankers. They sold the currency at an average advance of one-half of one per cent. Two classes of buyers chiefly furnished the demand. First, and most naturally, there were employers of labor with large weekly or monthly pay-rolls, whose deposits lay in banks which flatly refused to pay them cash for checks. Second, and more numerous than might have been supposed, there were banks which were unwilling to refuse cash payments, but which were not averse to paying a premium to replenish their cash reserves.

The first of these transactions makes the operation easy of analysis. Currency, it is said in common phrase, was bought with checks. But this statement involves an absurdity ; for nothing had happened to alter the value of the currency. The actual transaction was a sale of bank checks for money. Something had very obviously happened to make the checks less valuable than they had been before. At the bank on which they were drawn these checks were now worthless for the one purpose for which their makers drew them — conversion into coin and bills of small denomination. They were sold in Wall Street, therefore, for what they would bring in cash. Like irredeemable paper currency, their percentage of depreciation — in other words, the premium on the kind of money needed — was measured by the ratio of supply and demand, and by the probability of their ultimate cash redemption. The supply of such checks offered last year in exchange for currency was large. But on the other hand early resumption of full cash payment by the banks was universally expected, and the checks themselves, still being good for all banking transactions and exchanges through the New York clearing house, were as good as cash for the most of ordinary purposes. Therefore, the “premium” on currency never rose exorbitantly high.

But did this operation check individual hoarding of money ? Obviously not. Withdrawal of funds from banks which refused

cash payments ceased of course ; but withdrawals from other banks were doubled. The logic of the bank restriction, therefore, pointed, if sound, to nothing short of general suspension. Nor was this all. A large part of the regular and individual bank depositors of money were driven away at once. The chances that a man with \$100 currency will deposit it in bank, when the bank announces that it will not return the money on demand, and when the currency may be "sold" for \$102 in Wall Street, are certainly small. The argument that the banks were forced to refuse cash payment, *because* of the premium in Wall Street, utterly confuses cause and effect. Of course, after the premium was offered, there was a chance that a depositor would withdraw his \$100, sell it for \$102 in Wall Street checks, withdraw the \$102 against this check, sell it again, and so on *ad infinitum*. But this ignores the fact that the bank restrictions caused the currency premium. Had the banks all continued to pay cash, no premium would have been possible. It is astonishing that any one should question this. What Wall Street broker in his sober senses would pay a \$102 check for \$100 currency, when he could get \$102 money by presenting the same check at bank ?

Hoarding was certainly increased by the bank restrictions. Deposits of cash in banks almost wholly ceased, and domestic exchange was completely blocked. The experience of August proved beyond dispute the effect of the Wall Street premium. This premium undoubtedly brought to sight great quantities of previously hoarded currency.<sup>1</sup> But no sooner had this money

<sup>1</sup> For obvious reasons, it is very hard to arrive at any trustworthy estimate of the amount of money thus brought into the market. The Wall Street firm which did the largest proportion of the business estimates the amount of money which changed hands during the currency premium at \$15,000,000; but this, though based on personal experience, is largely guess-work. Some up-town retail stores sold their daily receipts of currency, a fact pretty publicly proved by the vigor with which other retail houses, in their advertisements at the time, boasted that they had regularly deposited their cash receipts in bank. There were, moreover, many sales of large blocks of currency, chiefly gold certificates, in lots as high as \$100,000, which had evidently been locked up in safe deposit vaults. It was a striking incident that on the death, several months before the panic, of a well-known New Yorker, a man of wealth and financial reputation, and a bank director, his executors found in his safe several hundred thousand dollars in gold

been exchanged and again disbursed, than it vanished once more from sight. No one who passed that month in New York City will dispute this. So completely, under the bank restrictions, did paper money disappear, that by the middle of August business of every kind was being done with specie, and people who in years had never touched a gold piece for their common uses were making daily payments in eagles and double-eagles. This money came not from the "purchases" from currency hoarders, but from the European gold importations. By the end of August practically all the banks had resumed full payment to depositors. But for a long time hardly any paper currency was paid; and how little the Wall Street purchases contributed to the recovery, the bank exhibits show. From August 5 to September 2—a period covering the existence of the currency premium—the specie holdings of the New York City banks increased by \$10,930,700.<sup>1</sup> But holdings of legal tenders increased only \$1,785,800, and deposits only \$1,064,900.

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certificates. The hoarding in New York was largely and perhaps chiefly speculative; in the interior, where it had far more serious effects, it was a natural result of the deposit and savings bank failures.

<sup>1</sup> The net gold import during July was \$5,776,401; during August, \$40,622,529. Much of this gold was, however, ordered by Chicago and Boston capitalists, and shipped direct to them. Still more was imported by Wall Street exchange bankers, and sold by them at a premium to savings-banks, corporations and business houses. The restriction on bank payments to depositors was the reason why no gold, except that ordered personally by bank officers, was deposited in the banks.